

Financial Forecast

This section includes:

- ▶ *Financial Forecast for FY 2005*
(Page 170)
- ▶ *Revenue Assumptions*
(Page 172)
- ▶ *Disbursement Assumptions*
(Page 174)

FINANCIAL FORECAST

FINANCIAL FORECAST

The Financial Forecast for FY 2005 has been developed in accordance with Budget Guidelines adopted by the Board of Supervisors on April 28, 2003. These guidelines serve as an important tool in the process of budget development. As resolved by the Board, the guidelines:

1. Limit the increases in County expenditures and the County's Transfer to the Fairfax County Public Schools to the projected rate of increase in revenues.
2. Require that available County balances, not necessary to support expenditures of a critical nature or to address the Board's policy on the Revenue Stabilization fund be held in reserve to offset future requirements.
3. Direct that non-recurring funds be allocated for non-recurring uses only.

The current Financial Forecast reflects these guidelines. In addition, as part of the FY 2005 Budget Guidelines, the Board requested that revised revenue estimates and current economic information be provided in late 2003 so that guidance can be given to the County Executive regarding the Real Estate Tax rate and the transfer to the Schools.

The current forecast projects County revenue growth of 4.97 percent in FY 2005. This rate of increase is due to moderating growth in residential property values, steady Revenue from the Commonwealth and modest growth in other revenue categories.

Current pressures faced by the County such as population growth, State budget cuts, and State mandates cannot easily be accommodated within the current level of revenue growth. Expanded health and safety requirements have added to the County's already strained resources. Additional service requirements have been necessary for public safety after the events of September 11th, the sniper attacks in fall 2002, and in the preparation for potential future terrorist attacks. Health concerns include the spread of West Nile virus and planning for contingencies such as mass smallpox inoculations. The County will continue to be challenged in order to balance these increasing service requirements and infrastructure needs within the constraints of projected revenue growth. The forecast for FY 2005 limits increases in County expenditures and the transfer to the Schools to the revenue growth rate anticipated in FY 2005 in accordance with the Board's guidelines; however, the forecast for FY 2005 shows a deficit of \$12.3 million. The FY 2005 forecast will be revised late in 2003 based on current projections of economic conditions and revised revenue projections. Based on these revised estimates and guidance from the Board of Supervisors, the FY 2005 budget will be developed and County spending will be adjusted to eliminate any deficit.

FINANCIAL FORECAST

FY 2005 FINANCIAL FORECAST

(millions)

	FY 2002 ACTUAL	FY 2003 ADOPTED	FY 2003 REVISED	FY 2004 ADOPTED	FY 2005 FORECAST
Available Beginning Balance	\$84.17	\$0.00	\$48.11	\$0.86	\$0.00
Reserves Balance	0.00	46.46	46.46	49.81	51.20
REVENUE:					
Real Estate Taxes	\$1,233.20	\$1,384.76	\$1,392.13	\$1,494.19	\$1,600.53
Personal Property Taxes ¹	471.46	469.24	469.63	477.17	488.88
Other Local Taxes	360.26	355.20	361.15	372.94	381.53
Permits, Fees, and Licenses	28.61	29.35	26.47	26.85	26.97
Fines and Forfeitures	10.32	11.00	9.71	12.04	12.41
Revenue from Use of Money/Property	28.23	32.74	16.31	16.37	17.42
Charges for Services	35.24	34.91	37.30	38.15	38.93
Revenue from the Commonwealth ¹	89.40	79.95	77.87	75.91	75.91
Revenue from the Federal Govt.	37.67	38.82	47.07	39.91	38.01
Recovered Costs/Other Revenue	5.90	5.68	5.30	5.40	5.50
TOTAL REVENUE	\$2,300.31	\$2,441.64	\$2,442.93	\$2,558.93	\$2,686.09
TRANSFERS IN	4.61	3.17	3.93	1.40	1.43
TOTAL RECEIPTS	\$2,304.93	\$2,444.80	\$2,446.85	\$2,560.33	\$2,687.52
TOTAL AVAILABLE	\$2,389.10	\$2,491.26	\$2,541.42	\$2,611.00	\$2,738.72
EXPENDITURES:					
Personnel Services	\$477.71	\$513.70	\$517.47	\$539.47	\$566.28
Operating Expenses	291.79	309.01	335.64	305.71	320.91
Worked Performed for Others	(29.44)	(31.80)	(33.08)	(38.11)	(40.01)
Capital Equipment	4.46	3.78	6.39	3.88	4.07
Fringe Benefits	110.43	120.67	128.52	134.62	141.31
TOTAL EXPENDITURES	\$854.95	\$915.37	\$954.94	\$945.56	\$992.56
TRANSFERS OUT:					
Schools	\$1,079.91	\$1,167.86	\$1,168.88	\$1,238.48	\$1,300.03
G O Debt (County)	98.01	100.09	100.09	98.45	104.50
G O Debt (Schools)	105.53	113.60	113.60	120.90	127.72
CSB	74.59	78.40	78.40	80.63	84.64
Metro	11.45	12.27	12.27	12.27	14.11
Paydown Construction	7.51	4.21	7.01	4.03	10.00
County Transit	16.06	16.74	17.94	20.28	22.28
Other Transfers	31.21	27.94	30.31	29.77	31.25
Information Technology	12.79	5.92	5.92	9.45	10.00
Revenue Stabilization	2.51	0.00	1.39	0.00	0.00
TOTAL TRANSFERS OUT	\$1,439.58	\$1,527.04	\$1,535.81	\$1,614.24	\$1,704.52
TOTAL DISBURSEMENTS	\$2,294.53	\$2,442.41	\$2,490.75	\$2,559.80	\$2,697.08
ENDING BALANCE	\$94.57	\$48.85	\$50.67	\$51.20	\$41.64
Managed Reserve	46.46	48.85	49.81	51.20	53.94
TOTAL AVAILABLE	\$48.11	\$0.00	\$0.86	\$0.00	(12.31)

¹ The portion of the Personal Property Tax reimbursed by the Commonwealth as a result of the Personal Property Tax Relief Act of 1998 is included in the Personal Property Tax category for the purpose of discussion in this section.

FINANCIAL FORECAST

REVENUE ASSUMPTIONS

FY 2005 revenue estimates are based on a review of current and projections of future economic conditions. The U.S. economy has not recovered from the downturn that began in 2001. Economic growth, as measured by the Gross Domestic Product (GDP) experienced a weak 1.6 percent increase in the first quarter of 2003. The future direction of the national economy is uncertain due in part to high national unemployment and unstable financial markets. Subdued economic growth is projected for the local economy. The Leading Index, designed to forecast the performance of the County's economy nine to twelve months in advance, has declined in the last three months erasing the small gains made over the past year. With the successful completion of the war in Iraq, consumer confidence and business investment are expected to rise in the coming months. Based on the recent trend in the Leading Index, the local economy may not start to advance until early 2004. Economic expansion will not immediately translate into improvements in revenue growth. As such, County revenue growth is expected to be constrained through FY 2005.

Total General Fund revenues are projected to increase 4.97 percent in FY 2005. This rate of growth over FY 2004 is the result of an anticipated moderation in Real Estate assessment increases, stabilization of Revenue from the Commonwealth and modest rates of growth in other revenue categories.

The Financial Forecast assumes an overall increase in Real Estate values of 7.15 percent in FY 2005 compared to the 12.48 percent increase experienced in FY 2004. Total equalization, or the reassessment of existing property, is anticipated to increase 5.41 percent in FY 2005. Housing in Fairfax County has experienced substantial price appreciation during the past two years driven by high demand, coupled with a tight supply, and low mortgage rates. Residential equalization rose 14.55 percent in FY 2004. Job growth in the County is expected to be slower than in the past several years, easing the demand for housing. Mortgage interest rates are anticipated to rise, reducing affordability. Residential equalization, therefore, is projected to increase a more moderate 7.50 percent in FY 2005.

In FY 2004, existing nonresidential property experienced an overall decline of 2.94 percent, the first decrease since FY 1996. Due to rising office vacancy rates, increased supply and recent sales activity, the value of mid- and high-rise office buildings, which comprise over 40 percent of the nonresidential tax base, fell 10.73 percent in FY 2004. The amount of sublet space on the market increased considerably during 2001. Space leased or purchased in anticipation of business expansion was no longer needed as the economy slowed. The Economic Development Authority reported that the office vacancy rate climbed to 12.1 percent as of year-end 2002, up from 6.4 percent at year-end 2001. Including sublet space, the office vacancy rate rises to 18.8 percent. The office vacancy rate is expected to rise over the next year as new buildings are completed. As a result of the increased space available, office property is expected to experience a slight decline in value in FY 2005. Hotel property experienced a 6.23 percent drop in value in FY 2004 after falling over 15 percent in FY 2003. Hotel occupancy rates are expected to slowly increase, but any growth in hotel values is expected to be slight. The Retail and Regional Malls categories rose moderately in FY 2004, increasing 2.91 and 6.95 percent, respectively. The abundance of retail space is anticipated to restrain the growth in these categories during FY 2005. Overall, the value of existing nonresidential properties is anticipated to experience a further decrease of 1.50 percent in FY 2005, primarily due to the office market in the County.

In addition to equalization, the remaining increase in Real Estate value is due to new construction or normal growth. New construction is expected to increase at a lower rate during FY 2005 as a result of economic conditions and a lack of buildable land in the County. Office construction will primarily be build-to-suit and no new hotel projects are anticipated. Residential construction is anticipated to be moderate. Overall, an increase of 1.74 percent due to new construction is projected for FY 2005 compared to an increase of 2.54 percent in FY 2004.

FINANCIAL FORECAST

The FY 2004 revenue estimate for Current Personal Property Tax revenue represents base growth of 2.4 percent, offset by an estimated \$1.4 million as a result of revisions to the County's FY 2004 depreciation schedule for computer equipment. In FY 2005, Personal Property Tax revenues, which represent 18.6 percent of total General Fund revenue, are expected to increase 2.5 percent. Both the vehicle and business components are anticipated to experience moderate growth in FY 2005 as business increases slightly and the vehicle market remains healthy.

Based on the Personal Property Tax Relief Act (PPTRA) of 1998, the Virginia General Assembly approved a plan to eliminate the Personal Property Tax on vehicles owned by individuals over a five-year period. In FY 1999, the first year of implementation, taxpayers were billed for the entire amount of tax levy and received a refund of 12.5 percent of the tax on the first \$20,000 of the value of their personal vehicle from the Commonwealth of Virginia. Vehicles valued less than \$1,000 were refunded 100 percent. In FY 2000, FY 2001, and FY 2002 through FY 2003, the PPTRA reduced the Personal Property Taxes paid by citizens by 27.5 percent, 47.5 percent, and 70 percent, respectively, with an offsetting reimbursement paid to the County by the Commonwealth. The percentage reduction in taxes paid by citizens is anticipated to remain at 70.0 percent in FY 2004. It should be noted that the PPTRA has no impact on the assessment or projection of total Personal Property Tax revenues; therefore, no assumption as to the rate of tax relief has been made for FY 2005.

Business activity and consumer spending are expected to be modest in FY 2005 and BPOL Tax revenues and Sales Tax receipts are both projected to rise 2.0 percent. Absent indicators of economic expansion, these categories have been held to the same rate of growth anticipated in FY 2004.

Interest earned on investments is expected to increase in FY 2005 based on a forecast of a slight rise in interest rates and growth in the investment portfolio. During CY 2000, the Federal Reserve lowered interest rates 11 times, leading to a significant reduction in the yield earned on the County's investment portfolio. The average annual yield on investments fell from 6.24 percent in FY 2001 to 2.58 percent in FY 2002. During CY 2002 the Federal Reserve held rates constant until November, when rates were reduced 50 basis points. Based on the current interest rates, the yield on County investments is expected to be 1.4 percent in FY 2003 and FY 2004. In FY 2005, the yield on investment is expected to rise slightly to 1.5 percent.

Excluding revenues from the Commonwealth of Virginia associated with the reimbursement of Personal Property Taxes, Revenue from the Commonwealth and Federal Government is expected to decline \$9.1 million, or 7.3 percent, in FY 2004. Of this reduction, \$3.4 million is the result of one-time Federal pass-through funding received in FY 2003 for child care services and \$2.7 million is due to a projected decrease in the illegal alien grant received from the Federal government as FY 2003 represented payments for 2 years. The remaining decrease is due to reductions in state aid used to help balance the Commonwealth's budget in FY 2004. In FY 2005, Revenue from the Commonwealth is anticipated to remain constant with the FY 2004 level. This estimate may be optimistic if State revenue does not increase and aid to localities is cut once again. Revenue from the Federal Government is expected to drop in FY 2005, as potential funding for localities holding illegal aliens may be eliminated.

Building and Permit fee revenue is anticipated to decline 9.6 percent in FY 2003. This revenue is a reflection of the construction industry, as well as the size and complexity of projects submitted for review. The slowdown in FY 2003 is indicated by current year-to-date revenues, a decline in major site and subdivision plans submitted, and a reduction in the number of building permits issued. In FY 2004 and FY 2005, Building and Permit fee revenue is projected to stabilize and remain at the FY 2003 level. It should be noted that the expectation that Building and Permit fee revenue will not increase assumes a continuation of the same level of building activity projected to be achieved in FY 2003 and should not be viewed as a further reduction.

FINANCIAL FORECAST

Revenue growth rates in these and other categories such as Vehicle Decals, Consumer Utility taxes and Charges for Services are shown in the following table:

REVENUE GROWTH RATES

Category	FY 2003	FY 2004	FY 2005
Real Estate Tax - Assessment Base	15.14%	12.48%	7.15%
Equalization	11.72%	9.94%	5.41%
Residential	16.27%	14.55%	7.50%
Nonresidential	0.52%	-2.94%	-1.50%
Normal Growth	3.42%	2.54%	1.74%
Personal Property Tax - Current ^{1,2}	1.33%	2.39%	2.50%
Local Sales Tax	-1.43%	2.00%	2.00%
Business, Professional and Occupational, License (BPOL) Taxes	0.00%	2.00%	2.00%
Recordation/Deed of Conveyance	15.63%	-28.70%	0.00%
Vehicle Decals	1.73%	2.34%	2.30%
Consumer Utility Taxes	0.65%	3.37%	2.00%
Building Plan and Permit Fees	-9.57%	0.00%	0.00%
Charges for Services	5.84%	2.27%	2.05%
State/Federal Revenue ¹	-1.69%	-7.30%	-1.64%
TOTAL REVENUE	6.20%	4.75%	4.97%

¹ The portion of the Personal Property Tax reimbursed by the Commonwealth as a result of the Personal Property Tax Relief Act of 1998 is included in the Personal Property Tax category for the purpose of discussion in this section.

² Including the adjustments to the computer depreciation schedule, Personal Property Tax revenues are anticipated to grow 0.23 percent in FY 2003 and 2.09 percent in FY 2004.

DISBURSEMENT ASSUMPTIONS

Direct Expenditures

As noted earlier, increases in County expenditures presented herein reflect the projected growth in County revenues. As such, direct expenditures increase 4.97 percent in FY 2005. The projected direct expenditure funding level, requirements associated with pay for performance, market rate adjustments, health insurance, retirement plan increases, and inflationary growth will leave little flexibility for expansion of services necessitated by population growth or new facilities. In order to provide for compensatory and inflationary increases, as well as cost requirements associated with future new facilities, reductions will be required in other parts of the County's budget in order to stay within the Budget Guidelines.

FINANCIAL FORECAST

Transfers Out

School Transfer

The Financial Forecast includes an increase in the School transfer consistent with the rate of revenue growth as directed by the Budget Guidelines.

Metro

The transfer requirements for Metro Operations and Construction reflect annual increases of 15.0 percent based on projected inflationary increases and infrastructure requirements for Metrorail and Metrobus service.

Debt Service

The Debt Service requirements reflect increases required to support the level of bond sales proposed in the FY 2004 - 2008 Capital Improvement Program (With Future Fiscal Years to 2013).

Paydown

Paydown capital construction includes transfers from the General Fund to support construction and renovation of capital projects. The projected annual transfer for paydown construction is \$10.0 million. It should be noted that the County's paydown construction program had been constrained in the early and mid-1990's based on budget limitations, deferring maintenance and repair costs and new construction of necessary public improvements. The projected level of paydown funding through FY 2005 will provide for essential maintenance and repair in order to protect and extend the operation of County facilities.

Transfer to Fairfax-Falls Church Community Services Board

The General Fund transfer supporting the Fairfax-Falls Church Community Services Board is consistent with the rate of revenue growth as directed by the Budget Guidelines.

Information Technology

The General Fund supports the County's investment in major Information Technology (IT) initiatives. Based on a recommendation from the County's Information Technology Advisory Group, the Financial Forecast includes a \$10.0 million IT transfer in FY 2005. The County's Information Technology Advisory Group (ITAG), a private sector advisory group established by the County Executive to investigate the condition of the County's IT resources, recommended significant increases in County support of the IT infrastructure. Identifying a total requirement of \$95 million, the ITAG recommended annual spending of \$15 to \$20 million.

Other Transfers/County Transit

An increase of 4.97 percent has been included for other transfers in FY 2005. A total of \$22.3 million is included for County Transit in FY 2005 based on a projected increase in costs associated with the CONNECTOR bus system and an increase in Commuter Rail contributions. The FY 2004 Adopted Budget Plan and the FY 2005 Forecast includes sufficient funding for the purchase of 15 replacement buses. Thereafter, annual funding in the amount of \$4.0 to \$5.0 million will be needed to provide for replacement of approximately 15 buses per year based on the age of the fleet and planned replacement.